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Stat Spotlight: Housing Backlog Hurt by Soft Appreciation

The great puzzlement of 1989 was why backlogs at the major multimarket homebuilding companies stayed so high in the face of weak housing starts, interest rate uncertainty and a laboring economy.

The great puzzlement of 1990 may be why backlogs are melting in the face of a still-strong economy.

We nominate "the Ghost of Appreciation Past" as the principal culprit.

In a nutshell, house prices aren't driving upward in many parts of the country — notably the Northeast, California and the Southwest — and hence new-house buyers haven't any strong incentives to buy. Some anecdotal evidence:

—"The steam has gone out of the market," says an executive of one housing company. "A year ago buyers felt that if they didn't sign up now, the price would be up \$5,000 in a month or two. They no longer feel that way."

—Cancellations are rising, especially in higher priced, move-up homes. Higher prices generally mean California or the Northeast, so it's not surprising to find the biggest slowdowns among merchant builders in these markets. Examples:

Newhall Land & Farming (NHL:NYSE), builder in many price ranges at its Valencia new town northwest of Los Angeles, says cancellations in its over-\$250,000 models left backlog about even in the March quarter.

Two California builders, **J.M. Peters** (JMP:ASE) and **Standard Pacific L.P.** (SPF:NYSE), reported new orders reached a low 35% and 15% of deliveries in their latest quarters (Feb. and Dec. respectively). This duo has the highest average selling price among major homebuilders, with JMP's average house selling for \$421,000 while SPF is a notch lower at \$291,500. SPF said March qtr. orders picked up however.

Toll Brothers Inc. (TOL:NYSE), the third highest-price builder in our survey with \$287,600 average price, interestingly is doing better in its Philadelphia and New Jersey markets with new orders running at 84% of its reduced delivery levels.

Taking a longer view, house price appreciation slowed by about 3.1% *per year* during the 1980s—which most people remember as a boomtime. Here's the statistical tale, based on median prices of merchant-built homes:

Years	Ending Median House Price	—% Change in—	
		Decade	Per Year
1970-79	\$ 62,900	+154.7%	+ 9.8%
1980-89	120,000	+ 90.8%	+ 6.7%

Price inflation seems to have slowed even more for existing homes, although the data are not quite as clear cut. However measured, slower appreciation strikes us the biggest reason why backlogs are melting ever so slowly for major homebuilders.

We profile the current state of the merchant housing market through the experience of 13 major homebuilders in tables I, II, and III on page 2. Table I shows that total deliveries in the four latest reported quarters slipped a bit to 54,098 units, or by 1.3% compared to the immediately preceding four quarters and by 3.0%

compared to year-ago quarters. A good part of this slippage traces to bad weather in the Northeast during December.

Table II shows that the 52,527 new housing contracts written in the four latest quarters fell 2.9% from the immediately preceding quarters and by 8.8% from the year-ago four quarters. Weather, plus seasonally weak housing sales, appear to be major causes. New orders were 65% of fourth-quarter deliveries, compared to 72%-73% replacement ratios in the fourth quarters of 1988 and 1987 respectively.

As a result of weaker sales, backlog of 19,905 units for the latest reported quarters fell 14.8% from the immediately preceding quarter and 7.1% from year ago numbers, as shown in Table III. Given the large seasonal swings in buyer habits, the year-to-year comparison is the more worrisome to us.

The March quarter, traditionally the strongest selling season for most builders, should be decisive in telling investors what kind of a year to expect for 1990. Early reports are mixed. Inside we size up housing market outlooks and earnings profiles for six of the 13 major multimarket builders, and will analyze the other seven in the next RSR issue.

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TABLE I - HOUSING UNIT DELIVERIES

Name	Sym.	Latest Month	Last 4 Quart.	Prev. 4 Quart.	Yr Ago 4 Quart.	% Change From—	
						Prev 4 Q	Yr. Ago 4 Q
Centex Corp.	CTX	Dec.	7,372	7,030	6,133	+4.9%	+20.2%
Del Webb Corp.	WBB	Dec.	1,392	1,058	792	+31.6%	+75.8%
Hovnanian Corp.	HOV	Nov.	3,180	3,205	2,876	-0.8%	+10.6%
J.M. Peters	JMP	Feb.	775	763	1,223	+1.6%	-36.6%
K&B Home	KBH	Feb.	5,705	5,736	5,017	-0.5%	+13.7%
Lennar Corp.	LEN	Feb.	4,128	4,259	4,116	-3.1%	+0.3%
NVR L.P.	NVR	Dec.	6,519	7,091	8,556	-8.1%	-23.8%
PHM Corp.	PHM	Dec.	5,849	6,453	6,887	-9.4%	-15.1%
Ryland Group	RYL	Dec.	9,215	9,113	9,354	+1.1%	-1.5%
Std.-Pacific L.P.	SPF	Dec.	1,443	1,423	1,756	+1.4%	-17.8%
Toll Bros.	TOL	Jan.	693	676	766	+2.5%	-9.5%
UDC-Univ. L.P.	UDC	Dec.	2,390	2,278	2,122	+4.9%	+12.6%
U.S. Home	UH	Dec.	5,437	5,747	6,178	-5.4%	-12.0%
TOTALS			54,098	54,832	55,776	-1.3%	-3.0%

TABLE II - NEW HOUSING CONTRACTS

Name	Sym.	Latest Month	Last 4 Quart.	Prev. 4 Quart.	Yr Ago 4 Quart.	% Change From—	
						Prev 4 Q	Yr. Ago 4 Q
Centex Corp.	CTX	Dec.	7,813	7,716	6,956+	+1.3%	+12.3%
Del Webb Corp.	WBB	Dec.	1,656	1,744	1,127	-5.0%	+46.9%
Hovnanian Corp.	HOV	Nov.	2,867	2,584	2,948	+11.0%	-2.7%
J.M. Peters	JMP	Feb.	759	838	1,043	-9.4%	-27.2%
K&B Home	KBH	Feb.	5,149	5,446	5,580	-5.5%	-7.7%
Lennar Corp.	LEN	Feb.	3,257	3,670	4,196	-11.3%	-22.4%
NVR L.P.	NVR	Dec.	6,068	6,399	8,207	-5.2%	-26.1%
PHM Corp.	PHM	Dec.	5,559	5,792	7,387	-4.0%	-24.7%
Ryland Group	RYL	Dec.	9,095	9,354	9,508	-2.8%	-4.3%
Std.-Pacific L.P.	SPF	Dec.	1,501	1,652	1,603	-9.1%	-6.4%
Toll Bros.	TOL	Jan.	717	704	653	+1.8%	+9.8%
UDC-Univ. L.P.	UDC	Dec.	2,491	2,514	2,263	-0.9%	+10.1%
U.S. Home	UH	Dec.	5,595	5,674	6,093	-1.4%	-8.2%
TOTALS			52,527	54,087	57,564	-2.9%	-8.8%

The 13 builders today sell at 6.2 times trailing 12-months EPS (Table IV), near the bottom of historic pricing norms. Current prices average a 24% premium over book value, with six (Hovnanian, J.M. Peters, Lennar, NVR, PHM and U.S. Home) selling below book value. As a group these 13 builders provide investors with 4.42% dividend yield, with the three master limited partnerships, or MLPs (NVR, Standard-Pacific and UDC-Universal) all yielding in double digits. Our basic rule is that when we start looking at homebuilders as yield stocks, it's generally time to buy the group. Comments on individual stocks:

Centex Corp. (CTX:NYSE), Dallas-

based diversified homebuilder, materials producer and contractor, has been the strongest stock performer among homebuilders because of its surging earnings. CTX is the nation's second largest homebuilder at 7,372 deliveries in calendar 1989. Its 20% gain in unit deliveries (Table I) is the second best percentage gain among builders, behind only Del Webb Corp. Better, new sales kept pace with a 12.3% gain in calendar 1989 (Table II), giving CTX a 20% gain in Dec. qtr. backlog to 2,622 DU (Table III) that is second only to WBB.

CTX's strength stems from two factors: (1) Diversification into most major metropolitan markets; and (2) Focus on

lower priced markets reflected by an average \$132,400 selling price (vs. \$144,100 for the 13 builders). EPS, derived 77% from housing, have kept pace and CTX likely earned about \$4.10/sh. in its March 1990 fiscal year. Unless housing tanks (which seems unlikely), CTX could earn \$4.50 in 1991. CTX shares have produced a 37% total return the past year and continue at A Rank and in Portfolio Planner.

Hovnanian Enterprises Inc. (HOV:ASE), builder of entry-level homes in the Northeast, mainly New Jersey, and Florida, continues under pressure in the stock market (see New Low list, page 4), reflecting expected poor results for its Feb.

TABLE III - DU BACKLOG AT END OF PERIOD

Name	Sym.	Latest Month	Last Quart.	Prev. Quart.	Yr Ago Quart.	% Change From—	
						Prev Q	Yr. Ago Q
Centex Corp.	CTX	Dec.	2,622	3,012	2,181	-12.9%	+20.2%
Del Webb Corp.	WBB	Dec.	900	1,017	636	-11.5%	+41.5%
Hovnanian Corp.	HOV	Nov.	1,884	1,881	2,308	+0.2%	-18.4%
J.M. Peters	JMP	Feb.	261	452	277	-42.3%	-5.8%
K&B Home	KBH	Feb.	1,723	1,525	2,279	+13.0%	-24.4%
Lennar Corp.	LEN	Feb.	1,507	1,423	2,378	+5.9%	-36.6%
NVR L.P.	NVR	Dec.	2,706	2,944	3,048	-8.1%	-11.2%
PHM Corp.	PHM	Dec.	1,453	1,792	1,694	-18.9%	-14.2%
Ryland Group	RYL	Dec.	3,126	4,254	3,246	-26.5%	-3.7%
Std.-Pacific L.P.	SPF	Dec.	587	1,036	529	-43.3%	+11.0%
Toll Bros.	TOL	Jan.	339	366	315	-7.4%	+7.6%
UDC-Univ. L.P.	UDC	Dec.	785	1,284	684	-38.9%	+14.8%
U.S. Home	UH	Dec.	2,012	2,376	1,854	-15.3%	+8.5%
TOTALS			19,905	23,362	21,429	-14.8%	-7.1%

TABLE IV - VALUE OF HOMEBUILDER STOCKS

Name	Sym.	Latest Month	Price	EPS Ratio	Price/Bk.Val.	Div.	Yld.	Equity/Share
Centex Corp.	CTX	Dec.	\$40.50	10.4	+44.1%	\$0.40	1.0%	\$28.11
Del Webb Corp.	WBB	Dec.	10.75	17.6	+41.9%	0.20	1.9%	7.58
Hovnanian Corp.	HOV	Nov.	5.38	5.7	-11.8%	0.00	0.0%	6.10
J.M. Peters	JMP	Feb.	8.00	4.4	-13.3%	0.00	0.0%	9.23
K&B Home	KBH	Feb.	13.25	5.8	+96.1%	0.30	2.3%	6.76
Lennar Corp.	LEN	Feb.	18.63	7.3	-27.9%	0.24	1.3%	25.85
NVR L.P.	NVR	Dec.	4.00	3.9	-9.6%	0.60	15.0%	4.43
PHM Corp.	PHM	Dec.	9.38	4.6	-22.4%	0.12	1.3%	12.08
Ryland Group	RYL	Dec.	20.00	6.2	+20.3%	0.60	3.0%	16.62
Std.-Pacific L.P.	SPF	Dec.	14.13	3.7	+47.7%	2.35	16.6%	9.56
Toll Bros.	TOL	Jan.	3.38	7.5	+18.2%	0.00	0.0%	2.85
UDC-Univ. L.P.	UDC	Dec.	23.63	4.7	+355.8%	2.80	11.9%	5.18
U.S. Home	UH	Dec.	1.13	37.5	-73.2%	0.00	0.0%	4.19
TOTALS			\$172.13	6.2	+24.2%	7.61	4.4%	\$138.53

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1990 fiscal year. HOV's deliveries rose 10.6% to 3,180 DU for the 12 months through Nov. 1989 (Table I) but new contracts fell modestly, by 2.7%, depressing backlog by 18.4% to 1,884 DU at the end of Nov. HOV expects a strong Feb. qtr. but acknowledges the softer New Jersey market has hurt. It no longer can sell from plans but must build model homes, and lotteries for entry-level urban projects have not yielded complete sellouts as in the past. HOV's \$111,300 average selling price puts it well below the major builder average. HOV earnings were hurt by 32¢/sh. value reserve for some Florida properties in the Nov. qtr. We believe HOV earned about \$1.00-\$1.10/sh. in its Feb. 1990 year. HOV cautions that further profit declines may occur in 1991. HOV is building income properties and sells 12% below book value. C Rank is continued.

J.M. Peters Co. (JMP:ASE), southern California builder of upscale single family homes, has been hurt by softening in its markets. JMP delivered 775 homes in its Feb. 1990 year, down 36.6% (Table I). New orders also fell so that year-end backlog of 261 homes is down only 6% (Table III). Gross profit margins shrank modestly, from 21.5% to 21.0% in the year. EPS fell 36% to \$1.81 per share, as anticipated. Fiscal 1991 EPS should be flat to down. JMP's future is uncertain since its control shareholder, San Jacinto Savings, is offering its control position for sale. San Jacinto in turn is controlled by Southmark Corp., the former real estate trading company planning to emerge from Chapter XI reorganization as an S&L holding company (p. 4). C Rank is held.

Kaufman & Broad Home Corp. (KBH:NYSE), entry-level homebuilder operating in California and France, has maintained forward momentum with deliveries up 13.7% year-to-year through Feb. New orders dropped 21% in the qtr. however and backlog stands 24% below year-ago levels (Table III). March orders picked up in California inland markets where KBH is strong. KBH also benefits from an expanding commercial building business in France. EPS seem to be peaking at about \$2.30/sh. and we see KBH as a less timely selection in our Portfolio Planner; A Rank is maintained.

Lennar Corp. (LEN:NYSE), a major Florida homebuilder which also operates in Phoenix, is basically flat at 4,128 deliveries in the 12 months through Feb. 1990 (Table I). Softer new order trends have cut backlog by 36.6% to 1,507 DU at the end of Feb. (Table III). But LEN is an old hand at rolling with volatile housing markets and typically inventories multifamily units during down times for resale when the market turns. LEN should benefit from an \$84,800 average sales price, lowest in this group. LEN's EPS have probably peaked for this cycle and we'd expect earnings of about \$2.25-\$2.40/sh.

for the Nov. 1990 fiscal year. LEN sells at a 28% discount to book value. Sound values and a conservative posture keep LEN at A Rank and a Portfolio Planner pick.

Del Webb Corp. (WBB:NYSE), retirement community builder in Phoenix, Tucson and Las Vegas, posted its first profits in four years for 1989, earning 61¢ per sh. after 21¢/sh. loss on discontinued gambling hotels. First year sales at Summerlin in Las Vegas boosted deliveries, backlog and net income. WBB has bought 1,200 acres near Palm Springs, Cal. for a fourth retirement community. We see modest EPS growth for 1990 and 1991.

MARKET PULSE: Realty Stocks Remain Gold *4/12/90* NEW HIGHS

In the first quarter of 1990, new lows outpaced new highs by nearly 12.5 to 1. This statistic bespeaks the market's current disdain for realty stocks, as one might expect in today's fundamentally weak real estate operating environment.

While most realty stocks have languished so far in 1990, the good news is that many of the most fundamentally strong stocks have held their ground. With top guidance and good dividend payout cushions, many of these stocks are excellent yield vehicles to weather the bottom of the current real estate cycle and a possible recessionary period, as in past cycles.

New High/Low Indicator: Although realty stock new lows have kept pace with the broad market, new highs have been laggards in this regard. This results from bad news (and press) which lately has come in bunches and outweighed any good news, which trickles in mostly on an individual company basis.

	New	New	Net	-% of All Stocks-	
Week	Highs	Lows	Highs	Highs	Lows
Apr. 12p	0	14	-14	NA	NA
Apr. 6	2	18	-16	0.6%	3.0%
Mar. 30	1	20	-19	0.3	4.3
Mar. 23	1	22	-20	0.3	4.7
Mar. 16	2	22	-20	0.6	5.7
Mar. 9	3	13	-10	0.9	3.6
Mar. 2	3	14	-11	1.2	2.5
Feb. 23	1	20	-19	0.7	3.5
Feb. 16	2	40	-38	0.9	7.3
Feb. 9	2	22	-20	0.8	4.3
Feb. 2	0	30	-30	0.0	3.0
Jan. 26	1	33	-32	0.5	3.2
Jan. 19	0	20	-20	0.0	3.2
Jan. 12	2	15	-13	0.5	3.9

In the two weeks ended April 6, three realty stocks hit new highs: Cedar Income Fund, Ltd., Major Realty and Pacesetter Homes, Inc. All are smaller special situations traded on NASDAQ.

Cedar Income Fund (CEDR: NASDAQ), a smaller equity trust managed by an Iowa life insurer, apparently is rebounding after shares were beaten down to 3-7/8 per share in the fourth quarter of 1989, 43% below a high of 6-3/4 at the beginning of the year. Cedar is in the process of digesting the assets of Cedar Income Fund 2 Ltd. following an Oct. 1989 merger, which boosted assets to \$19.6 mil. CEDR is working to fill 50% in vacancy and expiring leases at a 78,550 sq.ft. Jacksonville office. The current 8% yield should mark an upper limit to CEDR's rise, which seems a technical rebound.

Major Realty Inc. (MAJR: NASDAQ), developer of Major Center outside Orlando, Fla., hit a new high despite negative news. We speculate that rumors of a possible asset sale could be fueling Major's new highs. One scenario is the sale of Major's interest in the Galleria mixed-use project in Orlando, Fla. to joint venture partner Prudential Life. The joint venturers are negotiating on future of the partnership. Another is the sale of additional land at Major Center outside Orlando to MCA Corp., which acquired 312 acres from Major in 1981 where it will open its Universal Studio Tour attraction later this spring to go head-to-head with nearby Walt Disney World.

Pacesetter Homes Inc. (PACE:NASDAQ), southern Calif. homebuilder, posted a 76% increase in revenues and a 50% increase in assets for 1989. Earnings per share rose to \$2.43 from a \$0.49 per share loss in 1988. The big push for thinly traded Pacesetter stock is a potential management-led buy-out of the 1.508 mil. shares outstanding, mentioned as a possibility in PACE's 1989 10-K. Insiders already hold 48% of shares. A companion income property builder, Pacesetter Business Properties, included similar wording in its 10-K.

NEW LOWS

Groups containing new lows placed by order of magnitude held their position in March. By loosely based groups and number of new lows in each group, they are:

Equity REITs/Property Owners - 12: BRE Properties, EQK Realty Investors, Eastgroup Properties, Gould Investors L.P., HRE Properties, HealthVest, Income Opportunity Realty Trust, Koger Equity, Koger Properties, MSA Realty, Perini Investment Properties, Santa Anita Companies.

MSA Realty (SSS:ASE), a shopping center REIT managed by Mel Simon Assocs., fell after its previously announced portfolio sale was put on hold. We move SSS back into the equity group from liquidating.

EQK Realty, (EKR:NYSE), equity REIT owning offices and a shopping center, posted a \$0.20 per share loss and cash flow was off 9% to \$1.49 per share in 1989. Like MSA, EQK was unable to find acceptable prices for its properties under a Jan. 1989 liquidation proposal.

HRE Properties (HRE:NYSE) has announced a one-quarter dividend cut of 44% to \$0.25/sh. Storage Equities, not listed as a new low this time, has also announced such a cut.

The market is casting a skeptical eye on the ability of **Koger Equity** (KE:ASE), Jacksonville equity REIT which periodically buys suburban offices built by sponsor Koger Properties, to raise \$80 to \$100 mil. in new debt this year to fund scheduled 1991 property acquisitions from **Koger Properties** (KOG:NYSE).

Perini Investment Properties

(PNV:ASE), investment builder affiliated with general contracting giant Perini Corp., reported a 6% decline in net current value to \$24.81 per share.

Mortgage Lenders - 7: American Realty Trust, Angeles Mortgage Trust, Angeles Participating Mortgage Trust, Capstead Mortgage (Pref.), Commonwealth Mortgage, Countrywide Mortgage, Rockefeller Center Properties. Most in this group have been plagued by bad loans and diminishing spreads which could get worse before improving. **American Realty Trust** lowered its dividend 47% to \$0.20 per share quarterly.

Rockefeller Center Properties (RCP:NYSE), owner of a \$1.3 bil. convertible mortgage on the world class complex in Manhattan, reported mixed results for 1989. Rock Center's vacancies doubled to 3.8%, vs. 1.6% in 1988, with most of the increase coming in the Dec. qtr. Rock Center still has an 11% edge on the 85% mid-Manhattan vacancy rate. Appraised value of Rock Center fee and leasehold interests remained unchanged at \$1.8 bil., the first flat year for value of RCP's underlying property.

Rock Center's gross revenues came in 6% higher at \$226 mil. but included \$5 mil. in one-time special rights payments from tenants. Net operating income also rose 6%. The Center leased 271,000 sq. ft. to 169 tenants during 1989 at \$40-\$45/sq. ft. RCP estimates the Center will have limited releasing risk through 1993 as it rolls over only about 120,000 sq. ft. per year. But about 31% of space or 1.9 mil. sq. ft. comes up for renewal in 1994.

Syndicators - 5: Angeles Corp., Equitec Financial, VMS Mortgage Investment Fund, VMS Mortgage L.P., VMS Mortgage III L.P. Finances and the market have soured on most of these entities and near-term prospects are poor. VMS recently announced postponement and suspension of dividend payments on all its publicly traded MLP's and REITs.

Homebuilders - 3: Calton, Hovnanian Enterprises, Union Valley Corp. Soft N.J. markets and the credit crunch have hurt these homebuilders. Hovnanian has seen a considerable slowdown in its markets but

has sufficient liquidity to make it through. Calton posted a \$0.19 per share loss for 1989. Union Valley reported a \$0.20 per share loss and lost a \$100 mil. revolving credit agreement, due Aug. 1990.

Investment Builders - 1: Forest City Enterprises Class B, continuing a slide.

Land Developers - 1: General Development Corp. GDV filed Ch. XI Apr. 6th; a cash crunch developed when financing sources dried-up after General Development and officers settled a Federal indictment which could approach \$100 mil. over 25 years. We've kept GDV stock on our Avoid/Sell list since last fall and won't change for now. Bottom fishers may wish to look at GDV's debt: 12.875% debentures of 1995 trading at \$23.75, and 12.625% of 2005 trading at \$13.

In Chapter XI - 1: Southmark Corp. (SM:NYSE) shares continue to fall on news that SM agreed with creditors on a reorganization plan that gives current shareholders only 2% of the ongoing company, which will mainly be an S&L holding company. Preferred holders get 3% of new SM; subordinated debtholders 11.3%; senior subordinated debtholders 18.5%; and senior creditors 64.7%.

Advance/decline indicator: It is misleading to generalize poor performance in the overall realty stock universe from the New high/low table. Realty stocks have in fact moved closely in sync with the movement of all stocks. Net advances of realty stocks vacillates between strength and weakness in near proportion to their percentage of the broad market.

Week	Adv.	Decl.	Net - % of All Stocks-		
			Adv.	Adv.	Decl.
Apr. 6	54	86	-32	2.3%	2.7%
Mar.30	66	62	+ 4	2.4	2.3
Mar.23	54	84	-30	2.5	2.5
Mar.16	58	73	-15	2.0	3.0
Mar. 9	78	57	+21	2.4	2.6
Mar. 2	69	54	+15	2.1	2.5
Feb.23	55	81	-26	3.4	2.2
Feb.16	53	87	-34	2.0	3.1
Feb. 9	64	66	- 2	2.0	2.9
Feb. 2	68	71	- 3	2.6	2.4
Jan.26	24	117	-93	4.8	5.1
Jan.19	69	69	0	6.7	4.2
Jan.12	44	89	-45	5.5	4.5